Cytonn INVESTMENTS

Stanbic Holdings – Q1’2023

12th May, 2023

Below is a summary of Stanbic Holding’s Q1’2023 performance:

Balance Sheet	Q1’2022	Q1’2023	y/y change
Net Loans and Advances	206.5	230.3	11.5%
Government Securities	45.5	49.9	9.7%
Total Assets	**331.0**	**391.6**	**18.3%**
Customer Deposits	**235.1**	**291.0**	**23.8%**
Deposits Per Branch	**9.0**	**9.7**	**7.3%**
Total Liabilities	**282.5**	**335.5**	**18.8%**
Shareholders' Funds	**48.6**	**56.1**	**15.5%**

Key Ratios	Q1’2022	Q1’2023	% point change
Loan to Deposit ratio	87.8%	79.1%	(8.7%)
Return on average equity	16.2%	20.7%	4.5%
Return on average assets	2.3%	3.0%	0.7%

Income Statement	Q1’2022	Q1’2023	y/y change
Net interest Income	3.7	5.4	44.7%
Net non-interest income	3.0	5.7	89.3%
Total Operating income	**6.8**	**11.2**	**64.7%**
Loan loss provision	(0.5)	(1.1)	132.9%
Total Operating expenses	**(3.8)**	**(5.7)**	**47.0%**
Profit before tax	2.9	5.5	87.8%
Profit after tax	**2.1**	**3.9**	**84.3%**
Core EPS	**5.3**	**9.8**	**84.3%**

Income Statement Ratios	Q1’2022	Q1’2023	% point change
Yield from interest-earning assets	2.2%	2.8%	0.6%
Cost of funding	2.4%	2.8%	0.4%
Net Interest Margin	6.3%	7.2%	0.9%
Net Interest Income as % of operating income	55.3%	48.6%	(6.7%)
Non-Funded Income as a % of operating income	44.7%	51.4%	6.7%
Cost to Income Ratio	56.8%	50.7%	(6.1%)
CIR without LLP	49.6%	40.5%	(9.1%)
Cost to Assets	1.0%	1.2%	0.2%

Capital Adequacy Ratios	Q1’2022	Q1’2023	% points change
Core Capital/Total Liabilities	18.2%	16.9%	(1.3%)
Minimum Statutory ratio	8.0%	8.0%	
Excess	**10.2%**	**8.9%**	**(1.3%)**
Core Capital/Total Risk Weighted Assets	14.4%	14.6%	0.2%
Minimum Statutory ratio	10.5%	10.5%	
Excess	**3.9%**	**4.1%**	**0.2%**
Total Capital/Total Risk Weighted Assets	16.3%	17.8%	1.5%
Minimum Statutory ratio	14.5%	14.5%	
Excess	**1.8%**	**3.3%**	**1.5%**
Liquidity Ratio	40.0%	45.6%	5.6%
Minimum Statutory ratio	20.0%	20.0%	
Excess	**20.0%**	**25.6%**	**5.6%**
Adjusted Core Capital/Total Deposit Liabilities	**18.2%**	**16.9%**	**(1.3%)**
Adjusted Core Capital/Total Risk Weighted Assets	**14.4%**	**14.6%**	**0.2%**

Adjusted Total Capital/Total Risk Weighted Assets	**16.3%**	**17.8%**	**1.5%**

Income Statement

- Core earnings per share rose by 84.3% to Kshs 9.8, from Kshs 5.3 in Q1’2022, lower than our projected growth to Kshs 8.5 in Q1’2023, with the variance stemming from the lenders’ increased loan loss provision by 132.9% to Kshs 1.1 bn, from Kshs 0.5 bn in Q1’2022 which is in contrast to our projection of a 32.3% increase to Kshs 0.6 bn. The lender’s overall performance was driven by the 64.7% growth in total operating income to Kshs 11.2 bn, from Kshs 6.8 bn in Q1’2022. However, the performance was weighed down by a 47.0% growth in total operating expenses to Kshs 5.7 bn, from Kshs 3.8 bn in Q1’2022,
- The 64.7% growth in total operating income was mainly driven by a 89.3% increase in Non-Funded Income to Kshs 5.7 bn, from Kshs 3.0 bn in Q1’2022, coupled with a 44.7% growth in Net Interest Income (NII) to Kshs 5.4 bn, from Kshs 3.7 bn in Q1’2022,
- Interest income grew by 49.1% to Kshs 7.9 bn, from Kshs 5.3 bn in Q1’2022, mainly driven by a 46.6% growth in interest income from loans and advances to Kshs 6.0 bn, from Kshs 4.1 bn in Q1’2022. As such, the Yield on Interest-Earning Assets (YIEA) increased to 2.8% from 2.2% recorded in Q1’2022, mainly attributable to the faster 49.1% growth in interest income compared to a 20.0% increase in average interest earning assets to Kshs 285.5 bn, from Kshs 237.8 bn in Q1’2022,
- Interest expenses rose by 59.7% to Kshs 2.4 bn, from Kshs 1.5 bn in Q1’2022, driven by 43.6% increase in interest expense on customer deposits to Kshs 1.8 bn, from Kshs 1.3 bn in Q1’2022, coupled with a 188.3% increase in interest expense from deposits and placements to Kshs 0.3 bn in Q1’2023, from Kshs 0.1 bn recorded in Q1’2022. Consequently, Cost of funds (COF) increased by 0.4% points to 2.8%, from 2.4% recorded in Q1’2022, owing to a faster 31.6% increase in Trailing interest expense to Kshs 8.1 bn, from Kshs 6.2 bn recorded in Q1’2022, compared to a 13.3% increase in average interest bearing liabilities to Kshs 285.8 bn from Kshs 252.3 bn in Q1’2022.Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 0.9% points to 7.2% from 6.3% in Q1’2022, attributable to a 38.3% increase in trailing net interest income to Kshs 20.6 bn, from Kshs 14.9 bn recorded in Q1’2022 which outpaced the 20.0% growth in average interest earning assets,
- Non-Funded Income (NFI) increased by 89.3% to Kshs 5.7 bn, from Kshs 3.0 bn in Q1’2022, mainly driven by a 147.7% increase in the foreign exchange trading income to Kshs 4.3 bn, from Kshs 1.7 bn in Q1’2022, highlighting the group’s increased foreign exchange margins. Total fees and commissions increase by 17.7% to Kshs 1.4 bn, from Kshs 1.2 bn in Q1’2022. The revenue mix shifted to 49:51 from 55:45 for the funded to Non-funded income owing to the 89.3% growth in Non-Funded Income which outpaced 44.7% growth in the Net Interest Income,
- Total operating expenses increased by 47.0% to Kshs 5.7 bn, from Kshs 3.8 bn in Q1’2022, driven by 132.9% increase in loan loss provisions to Kshs 1.1 bn, from Kshs 0.5 bn recorded in Q1’2022, and coupled with a 75.7% increase in other expenses to Kshs 2.4 bn from Kshs 1.4 bn in Q1’2022. The increase in provisioning is partly attributable to rising credit risk as a result deteriorioted economic environment as evidenced by the average Purchasing Managers Index (PMI) of 49.3 in Q1’2023, down from an average of 50.3 in Q1’2022,
- Cost to Income Ratio (CIR) decreased to 50.7%, from 56.8% in Q1’2022, owing to the 64.7% increase in total operating income, which outpaced the 47.0% increase in total operating espense. Notably, CIR without LLP declined by 9.1% points to 40.5% from 49.6% recorded in Q1’2022 an indication of improved efficiency, and,
- Profit before tax increased by 87.8% to Kshs 5.5 bn, from Kshs 2.9 bn in Q1’2022, with effective tax rate decreasing to 29.2% in Q1’2023, from 33.9% in Q1’2022, leading to an 84.3% increase in profit after tax to Kshs 3.9 bn in Q1’2023, from Kshs 2.1 bn in Q1’2022.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 18.3% to Kshs 391.6 bn, from Kshs 331.0 bn in Q1’2022, driven by a 11.5% loan book expansion to Kshs 230.3 bn, from Kshs 206.5 bn in Q1’2022, coupled with a 192.9% increase in placemenets due from banking institutions to Kshs 28.3 bn, from Kshs 9.7 bn in Q1’2022. Additionaly, investment in government securities increased by 9.6% to Kshs 50.3 bn, from Kshs 45.9 bn in Q1’2022,

- Total liabilities rose by 18.8% to Kshs 335.2 bn, from Kshs 282.5 bn in Q1’2022, driven by a 23.8% growth in customer deposits to Kshs 291.0 bn, from Kshs 235.1 bn in Q1’2022, coupled with a 21.1% increase in borrowings to 14.8 bn, from Kshs 12.2 bn recorded in Q1’2022. With 29 branches countrywide and 1 branch in South Sudan, compared to 26 branches in Q1’2022, deposits per branch increased by 7.3% to Kshs 9.7 bn, from Kshs 9.0 bn in Q1’2022,
- The faster 23.8% growth in deposits as compared to the 11.5% growth in loans led to a decrease in the loan to deposits ratio to 79.1%, from 87.8% in Q1’2022,
- The group’s Asset Quality deteriorated, with Gross NPL ratio increasing to 11.7% in Q1’2023, from 11.1% in Q1’2022, attributable to 19.3% increase in Gross non-performing loans to Kshs 29.3 bn, from Kshs 24.6 bn in Q1’2022, which outpaced the 13.0% increase in gross loans to Kshs 249.8 bn, from Kshs 221.0 bn recorded in Q1’2022,
- General Provisions (LLP) increased by 35.9% to Kshs 13.2 bn in Q1’2023, from Kshs 9.8 bn in Q1’2022. The NPL coverage increased to 66.7% in Q1’2023, from 59.1% in Q1’2022, attributable to the 35.9% increase in provisions coupled with 31.8% increase in interest in suspense to Kshs 6.3 bn from 4.8 bn in Q1’2022, which offset the 19.3% increase in Gross Non-Performing loans,
- Shareholders’ funds increased by 15.5% to Kshs 56.1 bn in Q1’2023, from Kshs 48.6 bn in Q1’2022, supported by a 15.0% increase in retained earnings to Kshs 46.3 bn, from Kshs 40.2 bn in Q1’2022,
- Stanbic bank remains capitalized with a core capital to risk-weighted assets ratio of 14.6%, 4.1% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 17.8%, exceeding the statutory requirement of 14.5% by 3.3% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 14.6%, while total capital to risk-weighted assets came in at 17.8%, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.0%, and a Return on Average Equity (ROaE) of 20.7%.

Key Take-Outs:

1. **Strong earnings growth -** Core earnings per share (EPS) grew significantly by 84.3% to Kshs 9.8, from Kshs 5.3 in Q1’2022. The strong growth was mainly driven by the 64.7% growth in total operating income to Kshs 11.2 bn from Kshs 6.8 bn in Q1’2022,
2. **Increased Provisioning -** On the back of high credit risk occassione by the deteriorated business environment, the bank increased its provisions holdings to cover for the anticipated losses in the future, with its provisions increasing by 132.9% to Kshs 1.1 bn from Kshs 0.5 bn recorded in Q1’2022. The high credit risk is further evidenced by the 19.3% increase in bank’s gross non-performing loans to Kshs 29.3 bn in Q1’2023, from Kshs 24.6 bn recorded in Q1’2022. Consequently, the NPL coverage increased to 66.7%, from 59.1% recorded in Q1’2022, and,
3. **Revenue diversification** – The lender’s non-funded income (NFI) increased by 89.3% to Kshs 5.7 bn, from Kshs 3.0 bn in Q1’2022, mainly driven by a 147.7% increase in the foreign exchange trading income to Kshs 4.3 bn, from Kshs 1.7 bn in Q1’2022, highlighting the group’s increased foreign exchange margins. On the other hand, Net Interest Income (NII) recorded a 44.7% growth to Kshs 5.4 bn from Kshs 3.7 bn in Q1’2022. As such, the revenue mix shifted to 49:51 from 55:45 for the funded to Non-funded income owing to the 89.3% growth in Non-Funded Income which outpaced 44.7% growth in the Net Interest Income, pointing towards increased revenue diversification.

Going forward, the factors that would drive the bank’s growth would be:

- **Digital transformation**. The lender has capitalized on digital innovation for service delivery over the past two years to improve its operational efficiency, which has been a key factor in its financial performance. In FY’2022, the lender disclosed that 93.0% of customer’s transactions in 2022 were conducted through its digital channels.

In 2022 the bank introduced borderless banking, allowing its customers across East Africa to conduct transaction smoothly and in real time.

- In our view, as the group prepares to unveil its next three year strategy later this year, the sustained digital transformation is expected to remain pillar in driving its growth.

Valuation Summary

- We are of the view that Stanbic bank is a "buy" with a target price of Kshs 139.1 representing an upside of 35.5%, from the current price of 112.0 as of 12th May 2023, inclusive of a dividend yield of 11.3%.
- Stanbic Bank is currently trading at a P/TBV of 0.9x and a P/E of 4.9x vs an industry average of 0.7x and 3.4x respectively.